United States Court of Appeals

for the Second Circuit

APPELLANT'S REPLY BRIEF

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P/S

In The

United States Court of Appeals

For the Second Circuit

USAchem, Inc.,

Plaintiff-Appellant,

vs.

HOWARD A. GOLDSTEIN and HOWARD A. GOLDSTEIN d/b/a GOLD SEAL ASSOCIATES,

Defendant-Appellee.

On Appeal from the United States District Court for the Western District of New York

APPELLANT'S REPLY MEMORANDUM OF LAW

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APPELLANT'S REPLY MEMORANDUM OF LAW

Statement

This brief is submitted by appellant USAchem in reply to the appellee's memorandum of law.

ARGUMENT

POINT I

Appellee's arguments against the issuance of an injunction are misguided and misleading on questions both of law and fact.

The appellee cites *Purchasing Associates v. Weitz*, 13 NY 2d 267 (1963), as the chief authority for the policy of the State of

New York on the subject of when injunctions will issue to enforce restrictive covenants in employment agreements:

> If, however, the employee's services are deemed "special or extraordinary," then the covenant may be enforced by injunctive relief, if "reasonable" even though employment did not involve the possession of trade secrets or confidential customer lists.
>
> Id. at 272.

Now there are really three bases set forth for the granting of an injunction: (1) the possession of confidential customer information; (2) the possession of trade secrets, or (3) other circumstances which make the employee's services "special or extraordinary."

None of this is out of harmony with the Texas cases which have been cited in USAchem's earlier memorandum of law submitted to this Court, in which specialized training and the relationship of cordiality and confidence built up between the salesman and the customer give rise to injunctive relief. There is no discord either between the New York policy and the rule announced in other cases around the country (and cited in USAchem's earlier brief) phrased in terms of the salesman's "special relationship" with the customers.

There is nothing magic about these concepts: they have real practical meaning. Sometimes a salesman's knowledge and experience and relationships with his customers are such that his persisting to work his old territory effectively ousts his employer from established business. This results in a continuing and very likely permanent loss of customers.

It is simply not possible to assign any accurate dollar value to such a loss. There is the loss of business up to the time of trial. There is the value of customer relationships and future business appropriated by the former salesman. There is the time released to the salesman to compete for new business, and perhaps other

practical advantages, in shipping rates for example, that may result to him from having an established customer base appropriated from his former employer. Thus injunction becomes the only effective remedy.

USAchem has a strong case on this record under the law of New York as well as of Texas. USAchem urges Texas law upon the Court for good reasons: (1) because the sales representative's agreement invokes the law of Texas where USAchem has its home, (2) because that law is consonant with the policies of the State of New York, and (3) because it serves interests of practicality and fairness for this agreement, which is in effect in all parts of the country, to be governed by a constant and predictable body of law. But whichever body of law this Court applies it has good authority for reversing the District Court's refusal to grant an injunction.

Everything in this record points to the sort of irreparable, incompensable harm that warrants an injunction.

While the appellee's brief suggests that, "Every day was a new grind with little customer loyalty" (p. 7), Mr. Goldstein's course of conduct upon termination with USAchem does not demonstrate his belief in this proposition. He ignored most of the great commercial and industrial businesses in his own backyard and travelled back south into his old rural territory to sell. (pp. 372, 374, 380-384)

Eighty-one percent of his sales in the fifteen months after termination were to former customers. (pp. 191-194). Ninety-five percent of sales were in his former territory (p. 192), and ninety-five percent were of products which had the same uses as the USAchem products which he had formerly sold. (pp. 192-193) So, one cannot tell from Mr. Goldstein's behavior that he had no competitive advantage with his old customers; he behaved as if that were exactly what he had, and his sales backed him up.

Appellee is at pains to suggest also that Mr. Goldstein's successor, Mr. Dougherty, "[w]ithin a few months . . . was selling at a rate almost equal to and at times exceeding Goldstein's sales." (See p. 6 of respondent's brief). Apart from the fact, however, that Mr. Dougherty's total sales were swollen by a 6% increase, this representation is deeply misleading. Mr. Goldstein's total sales for 1971 were $67,510 (pp. 52-53) resulting in commission income to him of $19,117 (p. 53). Mr. Goldstein's commission income for the previous year was almost the same — $19,317 in 1970. In both years he sold more than the $60,000 posted by Mr. Dougherty in his first year on the job. Moreover, we know that Mr. Goldstein was out of work for three months in 1970 with a gall bladder operation. (p. 170-173) We know also that after 1970 he had lost his enthusiasm for his job with USAchem. Here is what he said of the period after he returned to work from his gall bladder illness (p. 173):

> Q. Did you continue to work the remainder of 1970? A. Yes, sir.
>
> Q. —— in the same manner in which you had worked in the past? A. I don't think I had as much enthusiasm, no. No. I didn't.

So the fact is that Mr. Goldstein, in the only years in which his sales and commissions can reasonably be compared with Mr. Dougherty's, was part of the time sick and the rest of the time working without enthusiasm. These facts changed his income, for back in 1969 he had earned commissions of $33,735; in 1968 commissions of $26,132; in 1967 commissions of $25,047. Mr. Dougherty did not do so well as Mr. Goldstein had done; he did not do nearly so well as Mr. Goldstein had done when Mr. Goldstein was really working. This is no discredit to Mr. Dougherty. Mr. Goldstein had appropriated most of the established business that ought to have been his.

What we have here is not isolated sales of products but an appropriation of USAchem's business. That appropriation is exactly the element that was needed to establish USAchem's right to an injunction. The validity of the contract had been upheld and it had been held violated. The wholesale taking away of USAchem's business by its former salesman was incontrovertably established in the record. Yet the Court below ignored this evidence and, it is respectfully submitted, erred by allowing the jury's finding with respect to the damages issue to govern the injunction issue. This "irreparable damage" was just the fact which the Court said it was looking for when it denied the preliminary injunction in July 1973 and indicated that "an injunction, granted at the conclusion of the trial," would be forthcoming when that element was established. Yet when such damage was proved beyond question the Court refused to look for it in the record.

The record makes it clear how wrong it is to say that Mr. Goldstein and Mr. Dougherty were on the same footing in this territory. Without an injunction to give Mr. Dougherty an opportunity to build a relationship with these old customers, they are likely lost to USAchem, and to Mr. Dougherty, forever. Only an injunction can cure this harm.

Finally, appellee's brief discusses certain cases relating to injunction in ways that are most misleading. These are:

——*National Chemsearch Corp. of New York, Inc. v. Bogatin*, 349 F. 2d 363 (3rd Cir. 1965). Among all the cases cited which uphold USAchem's restrictive covenant, appellee points to the U. S. Court of Appeals decision in the *Bogatin* case for the proposition that "The present employment agreement has already been declared unreasonable." The appellate decision in *Bogatin*, however, does not purport to say any such thing and, to anyone who gives the case some scrutiny, does not even seem to say such a thing.

While it is true that the Court of Appeals reversed the granting of a preliminary injunction and remanded the case for further disposition, the Court certainly did not hold that the granting of a preliminary injunction was improper or that another preliminary injunction should not be granted upon the remand or that the District Court's analysis of the law and facts relating to the injunction issue was incorrect. What it found improvident was the granting of a preliminary injunction "for a period of one year" rather than *pendente lite*.

What the District Court had done was to grant a one-year injunction based on the one-year contractual provision in issue; that is, the trial court granted the same injunction that would have been granted after a full-scale evidentiary hearing, upon an application for preliminary relief only. A preliminary injunction "is, by its very nature, interlocutory, tentative, provisional, ad interim, impermanent, mutable, not fixed or final or conclusive, characterized by its for-the-time beingness." 7 *Moore's Federal Practice* ¶ 65.04[1] The relief granted by the District Court was properly injunctive; what was improper was that it was not preliminary.

Thus, in *Certified Laboratories of Texas, Inc. v. Rubinson*, 303 F. Supp. 1014 (E.D. Pa 1969), the preliminary injunction granted *pendente lite* was not even challenged, though *Bogatin* had arisen in the same district four years before.

It was, then, the fixed duration of the preliminary injunction in the *Bogatin* case which ran afoul of the 3rd Circuit; and that is the one factor present in the *Bogatin* case which has no relevance to this case. The reasoning about the propriety of injunctive relief there was reaffirmed in *Rubinson*.

—*National Chemsearch Corp. v. Weinberg*, No. 68-CH-2698 (Circuit Court, Cook County, Ill., August 22, 1968) (unreported). At pages 30-31 of its brief, appellee sets forth "the following conclusions . . . entered by Judge Cohen after trial on

the merits: . . ." and four written conclusions follow, by which it is made to appear that the restrictive covenants in issue were simply held unreasonable and unenforceable. In actuality the four conclusions of law set forth in appellee's brief were only four of seven conclusions reached in this unreported decision.

The Court held the covenants unreasonable in time and extent only and not inherently unreasonable and unenforceable; then the Court went on to explain how it lacked the blue-pencil power, under the law of Illinois, to sever or modify the covenants so as to make them enforceable. *Then* the Court went on to reach the following conclusions of law:

> 5. The copies of the "route Book" retained by the defendant WEINBERG at the termination of his employment, constituted the property of the plaintiff corporation and contained confidential information with respect to the plaintiff's customers, their buying habits and personnel to which the defendant WEINBERG was not entitled, following the termination of his employment. Therefore, the continued solicitation of the plaintiff's customers by the defendant WEINBERG or others acting in behalf of the defendant corporations, constitute unfair competition per se.
>
> 6. Plaintiff is entitled to damages against the defendants jointly and severally for a period of approximately six and one-half months, that is, from February 1, 1968, to August 20, 1968, in an amount equal to 10% of the gross sales made by EDWARD WEINBERG during that period which sales were made to the customers whom he served while employed by the plaintiff.
>
> 7. Plaintiff has no adequate remedy at law to protect it against the defendant's use of the "route books" from the date of this order; therefore, an injunction to protect its accounts for a six month period is necessary and proper. This length of time the plaintiff has determined to be a reasonable length of time during which to protect the accounts of its salesmen from each other.

Thus while the Court found itself, under the special circumstances of that case, unable to tailor the restrictive covenant to the situation, it saw the need of an injunction to restrict conduct, exactly like Mr. Goldstein's, and it granted injunctive relief.

So should it be granted here.

POINT II

Mr. Goldstein is not entitled to a reversal of the judgment against him for draw checks which he cashed under false pretenses

The appellee's sales representatives' agreement with USAchem expressly provided for the payment of advances against commissions. There was nothing ambiguous about the contract on that score; the advances were in the nature of a loan secured by Mr. Goldstein's sales. The appellee's lawyers now argue that there was no agreement to repay, but Mr. Goldstein left no doubt during his own testimony that he knew what his agreement was. When he became ill with a gall bladder ailment in 1970 and was not working, he had the following conversation, as he described it on the stand, with Hal Kimmel, the vice president of USAchem (pp. 358-359):

> Q. Did you ever have any conversation at that time regarding the draws you were getting with Mr. Kimmel? A. Well, I don't think I saw Mr. Kimmel personally. He called me on the phone to see how I was doing. Yes, I did ask him. I mean, at that point I had never had a debit balance. I never had been in the red. I always made more money than my draw, so I received commission checks, but at this point, I was in the hospital three months, and I was concerned. I said, "Hal, you know after not working for three months, I am going to have a debit balance, and I'm going to owe some money here."

> I said, "My requirements aren't that great now, because I'm not working. I am in the hospital. I am laid up."
>
> He said, "Listen, what are you worrying about now? You are sick. Just get better. Leave the draws to me. I will take care of that. It is bookkeeping basically."
>
> Basically, that was it. He just wanted me not to be concerned about money.

Mr. Goldstein knew that if he collected draw money and sold nothing, ". . . I am going to owe some money here." Whatever Mr. Kimmel said about "bookkeeping" it is obvious that this conversation would never have occurred except upon the premise that Mr. Goldstein, laid up as he was, was about to get himself into debt. He knew that, and that is why he brought the subject up. What Mr. Kimmel did was not a denial of the contractual obligation but a forgiveness of it. However much Mr. Goldstein sought to muffle this fact during his testimony, it came through loud and clear.

There is something else to bear in mind in relation to appellee's argument that he should not have to pay back the 1972 draw money. The summer of 1972 was not a period, like early 1970 when he had his gall bladder operation, during which Mr. Goldstein was simply too sick to work and collected advances.

In the first place the appellee's own references to the "illness" of 1972, just prior to his leaving, raise suspicion about it. On the witness stand Mr. Goldstein stubbornly clung to the characterization of his ailment as something in the nature of a heart attack or a "warning" of a heart condition. (pp. 392-393) In the appellee's brief to this Court, the statement is made that ". . . Goldstein was again physically incapacitated for several months due to a cardiac problem . . ." (p. 5 of respondent's brief). Yet during an examination before trial (read into the trial record at page 177) Mr. Goldstein specifically stated that any "cardiac involvement" was "ruled out" when he went into the hospital in

June 1972. What is important is not whether Mr. Goldstein had symptoms that might have looked like a heart attack. Perhaps he did. Now, however, he is trying to give a false impression. This is of the same order of phenomena as referring to the contract as one of "a number of forms" he signed back in 1963 without paying any attention to it (pp. 350, 379-380). It is the same sort of thing as saying, as he does at page 359 of the record: "Earlier, when I was employed, it was understood that this [the commission advances] was just a bookkeeping thing" when in another breath he testified to his concern about repaying them. The appellee's characterizations are not always candid; one has to look behind them.

In the second place, the "several months" during which he claims to have been incapacitated with a "cardiac problem" were less than three months at most; and his incapacitation during that time did not keep him from methodically and secretly violating his contract by organizing his new business, lining up his sources of supply, trying to tempt other USAchem salesmen away and going back to work as soon as Gold Seal Associates was ready to do business. He systematically collected from USAchem money which he did not intend ever to try to earn. Not only was Mr. Goldstein in breach of his contract, but each cashing of those summer draw checks was a little act of fraud. Every time he cashed that check he was representing to USAchem, "I am still working for you"; and it was not so and he knew it was not so.

The judgment against him for $3,300 should stand.

POINT III

Appellee Goldstein's counterclaim relative to his alleged interest in the stock participation plan and profit sharing plan is without merit; those plans involve no contribution whatever by the employee and receipt of benefits under those plans is expressly and validly made contingent upon the employee's refraining from engaging in competition with the employer in violation of the sales representative's agreement.

The Stock Participation Plan for Members of the National Chemsearch Sales Organization provides at paragraph 13 as follows:

> 13. *Non-competition or Injurious Conduct.* Notwithstanding any other provision of this plan, whenever in its sole discretion the Committee shall determine that a Participant shall have, in the opinion of the Committee:
>
> (a) engaged directly or indirectly in competition with the Company or with any of its subsidiaries, whether as an employee, agent, advisor, owner or partner of, or in any other affiliation or connection with, any business so competing . . .
>
> * * * *
>
> Then in either of such events such Participant shall thereupon forfeit all benefits under this plan and shall have no further benefits hereunder . . .

Section 12.3 of the National Chemsearch Corporation Profit-Sharing Plan reads in relevant part as follows:

> . . . In the event that a Participant or Former Participant directly or indirectly competes with Employer, or enters into the Employment of any corporation doing business in direct or indirect competition with Employer, or has any direct or indirect competition with Employer, or has a direct or indirect ownership in such a corporation, partnership, proprietorship or other business

> organization, after severance of employment, such Participant shall forfeit all accounts remaining in such Participant's Individual Account . . .

These provisions are unambiguous, and the validity of such provisions has repeatedly been upheld in the courts of the State of New York. The leading case in this area of the law is *Kristt v. Whelan*, 4 A.D. 2d 195, 164 N.Y.S. 2d 239 (1st Dept. 1957), affd. without op. 5 N.Y. 2d 807 (1958). Here the plaintiff was a former employee and beneficiary of a profit-sharing plan, which, like the one in issue, provided for forfeiture of benefits under the plan should the employee-beneficiary "engage or be employed in any occupation or business which is in competition with the company . . ." The plaintiff voluntarily terminated his employment, and, like Mr. Goldstein, went into competition with his employer. The trustees of the plan accordingly forfeited his interest in the plan.

The plaintiff sued the trustees contending that the non-competition clause was against public policy and restrained competition. The Appellate Division, First Department, reversing and dismissing the complaint on the merits, said:

> This contention is without substance. It is no unreasonable restriction of the liberty of a man to earn his living if he may be relieved of the restriction by forfeiting a contract right or by adhering to the provisions of his contract . . .

Again in *Kidd v. Oakes*, 39 Misc. 2d 645, 241 N.Y.S. 2d 403 (1st Dept. App. Term 1963), the Court reversed the trial court (39 Misc. 2d 100, 240 N.Y.S. 2d 297) which had held that, because the non-competition provision of a profit-sharing plan was without limitation as to "time or place", it was void. Appellate Term disagreed in a *per curiam* opinion:

> The question raised by this appeal is whether plaintiffs may recover the benefit paid to defendant pursuant to a profit-sharing plan. While the contention is that the contract results in unlawful restraint, yet an

> employee may legally undertake a restriction of his liberty to earn his living if he, by the contract, may be relieved of the restriction by forfeiting a contract right or by adhering to the provisions of the contract . . .

The same geographical and temporal restrictions necessary in the noncompetition clause of the underlying employment agreement are not required in the noncompetition provision of the profit-sharing plan. The question is not one of a restriction upon a right to earn a living as consideration for giving employment but of an agreed restriction as part of a special benefit plan — which the employee is free to waive so long as he gives up the benefit.

See also *In Application of Kumm*, 36 Misc. 2d 816, 233 N.Y.S. 2d 598 (Sup. Ct. Niagara County 1962); *Kerpen v. First Investors Corporation*, 45 Misc. 2d 793, 257 N.Y.S. 2d 880 (Sup. Ct. N.Y. County 1965), stressing that a provision like the one in issue in this case was not a negative covenant prohibiting engagement in a similar business but a contractual provision controlling the compensation to be earned, a contract which the parties are free to make.

The federal courts when called upon to apply New York law in this area have applied it in the same way. *Jacobus v. Massachusetts Mut. Life Ins. Co.*, 91 F. Supp. 674 (W.D. N.Y. 1950); *Bradford v. New York Times*, Antitrust Regulation Reporter, Issue 627 at Pg. A7.

The profit-sharing and stock participation plans in the present case are, like the plans in the cases cited, non-contributory: the profit-sharing plan because Mr. Goldstein never contributed to it, and the stock participation plan because it was by its terms non-contributory. Mr. Goldstein had no money of his own in either program; National Chemsearch, predecessor of USAchem, voluntarily contributed all the funds that were in them. It was, therefore, entitled to postpone the actual payment of *a gift* upon the condition that he is not to

compete with his employer after leaving his employment. See especially, *Application of Kumm, supra.*

In any event, so far as the stock participation plan is concerned, the appellee, even if he were still with the company now, would not become entitled to benefits under the plan before the happening of one of four other conditions precedent — none of which has been fulfilled. Paragraph 12 of the plan provides that a participant becomes entitled to full benefits if:

> (a) he retires from employment with the Company or any of its subsidiaries at or after age 65, or
>
> (b) he retires from employment with the Company or any of its subsidiaries prior to age 65 but after age 59, with the approval of the Committee, or
>
> (c) he dies while employed by the Company or any of its subsidiaries, or
>
> (d) he completes (i) fifteen (15) years of employment with the Company or its subsidiaries before ceasing such employment and (ii) remains employed by the Company or its subsidiaries at least five years after the grant of the stock participation unit entitling him to benefit before ceasing such employment (but in no event shall benefits actually be paid out under this plan to a living participant until he shall have attained age 65 or shall have both attained age 59 and received the approval of the Committee for earlier payments).

None of these things has happened. Most particularly Mr. Goldstein did not work for the company or its subsidiaries for fifteen years before ceasing such employment.

As Mr. Goldstein declined to adhere to the terms of his sales representative's agreement, so he declined to preserve the conditions precedent to the vesting of his rights under the profit-

sharing and stock participation plans. Because he has done precisely the things which he expressly agreed not to do, his counterclaim is without merit and should in all respects be dismissed.

POINT IV

The amount of damages awarded does not retroactively invalidate the allegation of jurisdictional amount

USAchem sought damages in its complaint not only in the amount of $3,836.00 in unearned advances but also an accounting "of all commissions or profits received by [Mr. Goldstein] by reason of any sales to customers in behalf of himself or Gold Seal Associates . . ." It also alleged that the matter in controversy exceeded ten thousand dollars. Without knowing what were the nature and amount of Mr. Goldstein's sales of competing products to former customers, there was of course no way for USAchem at the outset of the case to calculate the exact damage figure it believed was owing to it.

On the other hand Mr. Goldstein's sales between August 1972 and November 1973 turned out to be $67,579.19 (p. 193), eighty-one per cent of which were to USAchem customers; and the value of an injunction with respect to future such sales was incalculable.

Professor Moore has said:

> It is settled that the amount actually recovered will not retroactively affect jurisdiction when the amount set out in the complaint was asserted in good faith, otherwise, jurisdiction would have to await final determination of the merits of the controversy.
>
> 1 Moore's Federal Practice ¶ 0.92[1]

Not only did the evidence adduced at trial document the good faith of USAchem's claim, but the fact that the District Court Judge sent the damage issue, on the question of lost profits, to

the jury, establishes the reasonableness and good faith of the allegation of the requisite jurisdictional amount.

This identical issue was ruled on in another District Court in *National Chemsearch Corp. of Missouri v. Schultz*, 173 U.S.P.Q. 218 (N.D. Ind. 1972), in a case involving this same contract. Here is what the Court said:

> "Under the test most favorable to this defendant, in an injunctive suit the amount in controversy is to be tested by the value sought to be gained by the plaintiff." *Glenwood Light and Water Co. v. Mutual Light, Heat and Power Co.*, 239 US 121 (1915); *Packard v. Banton*, 264 US 140 (1924).
>
> "Attempting to evaluate the monetary loss for the purposes of an injunction is extremely difficult, and, indeed, this is a primary reason why an injunction rather than an action at law for damages is necessary. However, considering the value of personal contacts in this industry; the possibility of irreparable loss of good will that could occur when a terminated salesman seeks to capitalize on the confidence customers have placed in him by relying on that confidence to solicit sales for competitors; the $1,534.36 liquidated sum, which plaintiff alleges is owed to it by the defendant; the evidence of sales already made by this defendant for the competitor; the remote possibility of alleged punitive damages, this court cannot say that it 'would appear to a legal certainty that the claim is really for less than the jurisdictional amount.'" See *Saint Paul Mercury Indemnity v. Red Cab Co.*, 303 US 282 (1938).

CONCLUSION

For the reasons set forth herein USAchem submits that it was entitled below to a judgment against the appellee, enjoining him for a period of eighteen months from competing with it by selling or soliciting sales of chemical specialty products within his former assigned territory, and USAchem therefore seeks a reversal of the denial of the judgment below and an order that such an injunction be issued, and for such other and further relief as to the Court may seem just and proper. The dismissal of appellee's counterclaim regarding the stock participation and profit-sharing plans ought likewise be dismissed.

Respectfully submitted,

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AFFIDAVIT OF SERVICE

July 12, 1974

RE: USAchem Inc. vs Howard A. Goldstein and Howard A. Goldstein d/b/a Gold Seal Associates

STATE OF NEW YORK)
COUNTY OF MONROE) ss.:
CITY OF ROCHESTER)

Johnson D. Hay , **being duly sworn, deposes and says:**

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(s)he personally served three (3) copies of the printed [Record] [Brief] [Appendix] of the above-entitled case addressed to: Appellant's Reply Memorandum of Law of the above-entitled case addressed to:

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Sworn to before me this 12th
day of July , 1974.

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State of New York, County of Monroe
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